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ND Mill and Elevator Association
Grand Forks, North Dakota

Audit Report for the Fiscal Years
Ended June 30, 2007 and 2006
Client Code 47500

Robert R. Peterson
State Auditor

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TABLE OF CONTENTS

For the Fiscal Years Ended June 30, 2007 and 2006

INDEPENDENT AUDITOR'S REPORT

Honorable John Hoeven, Governor

Members of the Legislative Assembly

The Industrial Commission

Vance Taylor, President and General Manager
North Dakota Mill and Elevator Association

We have audited the accompanying financial statements of the business-type activities of the North Dakota Mill and Elevator Association, an agency of the state of North Dakota, as of and for the years ended June 30, 2007 and 2006, as listed in the table of contents. These financial statements are the responsibility of the North Dakota Mill and Elevator Association's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of the North Dakota Mill and Elevator Association are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the business-type activities of the State of North Dakota that is attributable to the transactions of the North Dakota Mill and Elevator Association. They do not purport to, and do not, present fairly the financial position of the State of North Dakota as of June 30, 2007 and 2006, and the changes in its financial position and its cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the North Dakota Mill and Elevator Association as of June 30, 2007 and 2006, and the results of its operations and its cash flows, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 21, 2007 on our consideration of the North Dakota Mill and Elevator Association's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 5-8 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Robert R. Peterson
State Auditor

September 21, 2007

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Honorable John Hoeven, Governor

Members of the Legislative Assembly

The Industrial Commission

Vance Taylor, President and General Manager
North Dakota Mill and Elevator Association

We have audited the financial statements of the business-type activities of the North Dakota Mill and Elevator Association, an agency of the state of North Dakota, as of and for the year ended June 30, 2007, which collectively comprise the North Dakota Mill and Elevator's basic financial statements and have issued our report thereon dated September 21, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the North Dakota Mill and Elevator's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the North Dakota Mill and Elevator's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the North Dakota Mill and Elevator's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the North Dakota Mill and Elevator's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the North Dakota Mill and Elevator's financial statements that is more than inconsequential will not be prevented or detected by the North Dakota Mill and Elevator's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the North Dakota Mill and Elevator's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the North Dakota Mill and Elevator's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

This report is intended solely for the information and use of management, the Industrial Commission, the Governor, and the Legislative Audit and Fiscal Review Committee and is not intended to be and should not be used by anyone other than these specified parties.

Robert R. Peterson
State Auditor

September 21, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of North Dakota Mill and Elevator Association's annual financial report presents the Mill's discussion and analysis of the Mill's financial performance during the fiscal year that ended June 30, 2007. Please read this information in conjunction with the financial statements that follow this section.

FINANCIAL HIGHLIGHTS

Condensed Financial Data

	Fiscal Year 2007	Fiscal Year 2006	Fiscal Year 2005
Current Assets	$ 42,315,299	$ 30,446,167	$ 29,874,630
Noncurrent Assets	211,663	125,547	100,201
Capital Assets	35,519,571	34,193,250	29,631,416
Total Assets	$ 78,046,533	$ 64,764,964	$ 59,606,247
Current Liabilities	$ 22,257,096	$ 9,068,186	$ 9,921,004
Noncurrent Liabilities	652,720	641,333	622,165
Total Liabilities	$ 22,909,816	$ 9,709,519	$ 10,543,169
Invested in Capital Assets, Net of Related Debt	$ 35,513,586	$ 34,199,235	$ 29,637,401
Unrestricted	19,623,131	20,856,210	19,425,677
Total Net Assets	$ 55,136,717	$ 55,055,445	$ 49,063,078
Operating Revenue			
Gross Sales	$ 164,915,600	$ 136,320,038	$ 127,223,085
Sales Deductions	(32,964,251)	(28,999,388)	(26,195,309)
Net Sales	$ 131,951,349	$ 107,320,650	$ 101,027,776
Nonoperating Revenue			
Interest Income	25,357	36,101	29,234
Miscellaneous	105,303	59,266	55,717
Total Revenues	$ 132,082,009	$ 107,416,017	$ 101,112,727
Operating Expenses			
Material Cost	$109,953,723	$ 85,717,907	$ 80,054,042
Manufacturing	13,980,705	12,816,918	12,498,283
Selling	1,070,031	1,006,459	1,001,422
General	1,366,565	1,228,385	1,161,047
Nonoperating Expenses			
Interest Expense	547,402	345,234	205,919
Loss on Sales of Assets		26,117	
Other	49,118	49,437	385,857
Total Expenses	$ 126,967,544	$ 101,190,457	$ 95,306,570
Revenue Over Expenses	$ 5,114,465	$ 6,225,560	$ 5,806,157
Transfer to Industrial Commission	(33,193)	(33,193)	(28,782)
Transfer to General Fund	(5,000,000)		(5,000,000)
Transfer to Department of Commerce		(200,000)	
Change in Net Assets	$ 81,272	$ 5,992,367	$ 777,375
Beginning Net Assets	55,055,445	49,063,078	48,285,703
Ending Net Assets	$ 55,136,717	$ 55,055,445	$ 49,063,078

- Gross sales reached a new record of $164,916,000 surpassing last year's gross sales record of $136,320,000.
- During the fiscal year, the Mill shipped 9,974,000 hundredweight of flour.
- Profits for the year were $5,114,000 falling short of last year's profits of $6,226,000.
- Mill operations provided more than $124,922,000 to the region and another $289,819,000 in secondary economic activity for a total economic impact of more than $414,741,000.

RESULTS OF OPERATIONS

Certain operating information is set forth below, as a percentage of gross sales for the fiscal years ended June 30, 2007, June 30, 2006 and June 30, 2005:

	FY 2007	FY 2006	FY 2005
Gross Margin	13.3%	15.8%	16.5%
Material Costs	66.7%	62.9%	62.9%
Operating Costs	10.0%	11.0%	11.5%
Profits	3.1%	4.6%	4.6%

Gross sales reached $164,916,000 for the fiscal year compared to $136,320,000 last year and $127,223,000 in fiscal year 2005. These record sales can be attributed primarily to higher wheat prices and the increase in flour shipments that were 629,000 hundredweights higher than last year and 847,000 hundredweights over fiscal year 2005. Sales of spring wheat flour were 9,035,000 hundredweight or 91% of our total sales while sales of durum products were 939,000 hundredweight. This compares to sales of 8,346,000 hundredweight of spring wheat flour and 1,000,000 hundredweight of durum products last year. Bulk flour sales represent 73% of the flour sold. Flour packed in bags accounted for 27% of the flour sold.

As a result of this sales volume, the Mill spent more than $105,774,000 buying spring wheat and durum. This is up from the previous year purchases of $75,298,000 and purchases in fiscal year 2005 of $70,496,000. This increase in fiscal year 2007 is due primarily to an increase of $1.03 in the price of grain delivered to the Mill during the year over the price paid in fiscal year 2006 and the increase in bushels of grain purchased. The Mill purchased more than 21,700,000 bushels of wheat and durum during the year just ended. Purchases of spring wheat and durum represented 96% of the material costs for the year compared with 88% during the past two years. The majority of the grain purchased is from North Dakota growers or grain elevators. No spring wheat or durum is purchased from Canada.

In addition to spending over $105,774,000 on grain, most of which went to North Dakota farmers, the Mill also spent $10,496,000 with other North Dakota based suppliers. Payroll costs for the North Dakota Mill were $8,652,000 for the year ended June 30, 2007. These three items when added together show that the Mill provided a direct economic impact to the region of over $124,922,000. A North Dakota State University study stated that for every dollar in direct economic activity from wheat processing, another $2.32 was generated in secondary economic activity. Thus, the Mill produced $289,819,000 in secondary economic activity resulting in a total economic impact of more than $414,741,000.

Operating costs rose to $16,417,000 compared to $15,052,000 last year and $14,661,000 in fiscal year 2005. This is an increase of $1,365,000 over last year. The primary cause for this increase in operating cost is due to an increase in production of 754,000 hundredweights as well as increases in the cost of energy and utilities and inflationary increases in other expenses. Operating cost per hundredweight of production increased to $1.66 from $1.65 in fiscal year 2006 and $1.64 in fiscal year 2005.

Gross margins as a percent of gross sales fell to 13.3% from 15.8% in fiscal year 2006 and 16.5% in fiscal year 2007. Excess capacity in the industry and competition is keeping downward pressure on margins. Profits as a percent of gross sales declined to 3.1% compared to 4.6% in each of the prior two years. Profits came in at $5,114,000, which is $1,112,000 below last year and $692,000 less than in fiscal year 2005.

LIQUIDITY

The North Dakota Mill's cash requirements relate primarily to capital improvements and a need to finance inventories and receivables based on raw material costs and levels. These cash needs are expected to be fulfilled by the Mill through operations and an established operating line of credit with the Bank of North Dakota. The Mill has a $17,000,000 operating line of credit with the Bank of North Dakota.

CASH FLOWS FROM OPERATIONS

Operating activities for the year ended June 30, 2007 used cash of $5,242,000 compared to providing cash of $9,612,000 in fiscal year 2006 and $8,326,000 in fiscal year 2005. The use of cash was driven by increases in the level of accounts receivables and inventories. Operating income for this same period was $5,580,000 compared to $6,551,000 and $6,313,000, in the prior two years, respectively.

CASH FLOWS FROM FINANCING ACTIVITIES

The North Dakota Mill had $17,000,000 of short-term debt outstanding and payable to the Bank of North Dakota on June 30, 2007 compared to $4,600,000 last year and $7,000,000 in fiscal year 2005. The Mill had no long-term debt outstanding at year-end. The increase in short term debt outstanding was used to fund current assets, specifically grain inventories, and accounts receivables.

NET ASSETS

Current assets increased $11,869,000 over last year and $12,441,000 over fiscal year 2005. This increase is due primarily to large increases in accounts receivables and inventories. Accounts receivables increased $6,225,000 while inventories climbed $5,914,000 from last year's values. This increase is primarily due to the increase in the price of wheat.

The carrying value of capital assets increased $1,326,000 to $35,520,000 for the year ended June 30, 2007. The North Dakota Mill completed several capital projects throughout the year that improved plant efficiencies and/or helped keep operating costs down. For more detailed information regarding capital assets and long-term debt activity see the Notes to the Financial Statements.

Current liabilities increased $13,189,000 from last year. The major change occurred in notes payable which grew $12,400,000. The notes payable is to the Bank of North Dakota. The total net assets increased by $81,000, resulting in an improvement in overall financial position. It is anticipated that the Mill will make its transfer to the general fund for the 2007-2009 biennium in June 2009.

COMMODITY PRICE RISK

The North Dakota Mill utilizes futures contracts offered through regulated commodity exchanges to reduce risk. The Mill is exposed to risk of loss in the market value of inventories and fixed purchase and sales contracts. To reduce this risk, opposite and offsetting futures positions are taken. Gains and losses on these positions are recognized for financial reporting purposes when they are realized.

INDUSTRY

U.S. per capita annual flour consumption increased slightly in 2006 to 134.2 pounds from 133.9 pounds in 2005. This is down from the 1997 peak of about 147 pounds per person per year due to the popularity of low carbohydrate diets. Due to yearly increases of the U.S. population, total 2006 flour disappearance is about flat with 1997 at just over 402 million hundredweight. Excess flour milling capacity and high wheat and durum prices continue to put downward pressure on margins. Demand for whole wheat and organic products continue to increase. National public interest in low carbohydrate diets continues to decrease.

North Dakota farmers again produced an excellent spring wheat crop this year. This has a positive impact on product quality and contributes positively towards increased profitability.

COMPARATIVE STATEMENT OF NET ASSETS
June 30, 2007 and 2006

		2007		2006
ASSETS				
Current assets:				
Cash and cash equivalents			$	77,856
Notes receivable				295,100
Receivables, net	$	26,243,207		20,017,847
Inventories		15,517,070		9,603,215
Prepaid expense		555,022		452,149
Total current assets	$	42,315,299	$	30,446,167
Noncurrent assets:				
Patronage capital credits	$	198,513	$	112,397
Other assets		13,150		13,150
Capital assets, net (note 6)		35,519,571		34,193,250
Total noncurrent assets		35,731,234		34,318,797
Total assets	$	78,046,533	$	64,764,964
LIABILITIES				
Current liabilities:				
Checks issued in excess of cash	$	1,507,665		
Accounts payable and other liabilities (note 7)		3,749,431	$	4,468,186
Notes payable		17,000,000		4,600,000
Total current liabilities	$	22,257,096	$	9,068,186
Noncurrent liabilities:				
Compensated absences	$	652,720	$	641,333
Total noncurrent liabilities		652,720		641,333
Total liabilities	$	22,909,816	$	9,709,519
NET ASSETS				
Invested in capital assets, net of related debt	$	35,513,586	$	34,199,235
Unrestricted		19,623,131		20,856,210
Total net assets	$	55,136,717	$	55,055,445

The accompanying notes are an integral part of the financial statements.

COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
For the Fiscal Years Ended June 30, 2007 and 2006

	2007	2006
OPERATING REVENUES		
Net sales	$ 131,951,349	$ 107,320,650
Total operating revenues	$ 131,951,349	$ 107,320,650
OPERATING EXPENSES		
Material cost	$ 109,953,723	$ 85,717,907
Manufacturing	13,980,705	12,816,918
Selling expense	1,070,031	1,006,459
General and administrative expense	1,366,565	1,228,385
Total operating expenses	$ 126,371,024	$ 100,769,669
Operating income	$ 5,580,325	$ 6,550,981
NONOPERATING REVENUES (EXPENSES)		
Interest income	$ 25,357	$ 36,101
Interest expense	(547,402)	(345,234)
Miscellaneous income	105,303	59,266
Loss on sale of capital assets		(26,117)
Other expense	(49,118)	(49,437)
Total nonoperating expenses	$ (465,860)	$ (325,421)
Income before transfers	$ 5,114,465	$ 6,225,560
Transfer to state general fund	$ (5,000,000)	
Transfer to Industrial Commission	(33,193)	$ (33,193)
Transfer to Department of Commerce		(200,000)
Change in net assets	$ 81,272	$ 5,992,367
Total net assets - beginning	55,055,445	49,063,078
Total net assets - ending	$ 55,136,717	$ 55,055,445

The accompanying notes are an integral part of the financial statements.

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COMPARATIVE STATEMENT OF CASH FLOWS
For the Fiscal Years Ended June 30, 2007 and 2006

	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers and users	$ 158,690,240	$ 133,488,058
Payments to suppliers	(155,291,365)	(115,996,968)
Payments to employees	(8,641,001)	(7,878,591)
Net cash provided (used) by operating activities	$ (5,242,126)	$ 9,612,499
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Proceeds from noncapital debt	$ 21,900,000	$ 8,600,000
Principal paid on noncapital debt	(9,500,000)	(11,000,000)
Note repaid for other than capital purposes	295,100	224,126
Interest paid on noncapital debt	(547,402)	(345,234)
Ag promotion	(49,118)	(49,437)
Other income	105,303	59,266
Transfer to state general fund	(5,000,000)	
Transfer to Industrial Commission	(33,193)	(33,193)
Transfer to Department of Commerce		(200,000)
Negative cash balance implicitly financed	1,507,665	
Net cash provided (used) by noncapital financing activities	$ 8,678,355	$ (2,744,472)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchases of infrastructure and equipment	$ (42,095)	$ (55,020)
Acquisition and construction of capital assets	(3,497,347)	(6,805,420)
Proceeds from sales of capital assets		7,520
Net cash used by capital and related financing activities	$ (3,539,442)	$ (6,852,920)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest income on investments	$ 25,357	$ 36,101
Net cash provided by investing activities	$ 25,357	$ 36,101
Net increase (decrease) in cash and cash equivalents	$ (77,856)	$ 51,208
Cash and cash equivalents, beginning	77,856	26,648
Cash and cash equivalents, ending	$ -	$ 77,856
Reconciliation of operating income to net cash provided (used) by operating activities:		
Operating income	$ 5,580,325	$ 6,550,981
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	2,213,121	2,264,969
Increase in receivables, net	(6,225,360)	(2,831,980)
(Increase) decrease in inventories	(5,913,855)	2,106,566
Increase in prepaid expense	(102,873)	(19,042)
Increase in patronage capital credits	(86,115)	(25,346)
(Decrease) increase in accounts payable	(1,179,944)	1,340,682
(Decrease) increase in accrued payroll	(4,098)	50,343
Increase in other liabilities	461,856	159,978
Increase in accrued sick and vacation pay	14,817	15,348
Total adjustments	$ (10,822,451)	$ 3,061,518
Net cash provided by operating activities	$ (5,242,126)	$ 9,612,499

The accompanying notes are an integral part of the financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies, as summarized below and the financial statements for the North Dakota Mill and Elevator Association (Mill) are in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB) which is the nationally accepted standard-setting body for establishing governmental accounting and financial reporting principles.

A. Reporting Entity

For financial reporting purposes, the Mill has included all of its operations as enterprise funds, and has considered all potential component units for which the Mill is financially accountable and other organizations for which the nature and significance of their relationship with the Mill are such that exclusion would cause the Mill's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. This criteria includes appointing a voting majority of an organization's governing body and (1) the ability of the Mill to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Mill.

Based upon these criteria, there are no component units to be included within the Mill as a reporting entity and the Mill is included within the State of North Dakota as a reporting entity.

B. Basis of Presentation

The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The Mill's activities are considered to be an enterprise fund, single business-type activity (BTA) and accordingly, are reported within a single column in the basic financial statements.

C. Basis of Accounting

The enterprise fund is accounted for on a flow of economic resources measurement focus. The accrual basis of accounting is utilized by the enterprise fund. Revenue is recognized at the time of shipment from the Mill or from the transloading site. Expenses are recognized at the time goods and services were received and accepted.

In accordance with GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, the Mill does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, for business type activities, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

D. Cash and Cash Equivalents

This classification appears on the Comparative Statement of Net Assets and the Comparative Statement of Cash Flows and includes petty cash and cash on deposit with the Bank of North Dakota. Cash and cash equivalents for reporting purposes includes cash and short-term, highly liquid investments that are readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. This includes investments with original maturity of three months or less.

E. Receivables

Accounts receivable represent amounts due from customers for credit sales. Other receivables consist of grain margin accounts, pending railway claims and amounts due from the Head Miller. The grain margin accounts are used to buy and sell spring wheat futures contracts on the Minneapolis Grain Exchange. Any activity would be recognized at cost after the settlement period. The allowance method is used to account for estimated uncollectible accounts receivable.

F. Inventories

Grain committed to production is valued at cost. Grain committed to sale is valued at net commitment price. Excess grain inventories are valued at June 30 Minneapolis grain market values less freight costs to Minneapolis. Flour, feed, and resale inventories are valued at ingredient cost plus manufacturing costs incurred in their production. Supplies inventories are valued at cost. The first-in, first-out basis is used for all inventories.

G. Capital Assets

Capital assets are stated at cost. When it is determined that a project consisting of machinery, equipment, or buildings will span more than one year, a “construction in progress” project folder is established to facilitate the accumulation until completion. Upon completion, the completed item is transferred to the applicable asset category. Movable equipment with a cost of $5,000 or more is capitalized and reported in the accompanying financial statements.

Depreciation is computed on a straight-line basis over the estimated useful life of the assets, generally 10 to 20 years for infrastructure, 30 to 40 years for buildings, 5 to 25 years for plant equipment, 7 to 10 years for office equipment and furniture and 5 to 10 years for leasehold improvements.

H. Noncurrent Long-Term Liabilities

Noncurrent long-term liabilities include compensated absences that will not be paid within the next fiscal year.

I. Compensated Absences

Annual Leave - Union employees earn vacation within a range of 6 days to 30 days per year depending on length of continuous service. Employees earn annual leave in a calendar year to be used during the next calendar year. Other employees are entitled to earn annual leave, based on tenure of employment, within a range of 12 days to 30 days per year. Individuals may bank earned vacation time to a total accumulation of 30 days payable at retirement or upon severance of employment.

Sick Leave - Union employees earn sick pay at the rate of one day for each two months of continuous employment. Upon termination, union employees shall be paid an amount equal to $50 times the total unused days of accumulated leave, not to exceed $5,000. Other employees earn sick pay at the rate of one day per month. Upon termination, these employees are entitled to be paid 10% of their accumulated sick leave, if employed 10 years or longer.

J. Storage Liabilities

Stored grain is treated as a reduction in inventory balances.

K. Net Assets

The Mill's net assets are classified as follows:

Invested in Capital Assets, Net of Related Debt – This represents the Mill's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Unrestricted Net Assets – Unrestricted net assets include resources derived from customer sales.

L. Revenue and Expense Recognition

The Mill presents its revenues and expenses as operating or nonoperating based on recognition definitions from GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*. Operating activities are those activities that are necessary and essential to the mission of the Mill. Operating revenues include all charges to customers. Revenues from interest income, gains on sale of capital assets, and bad debt recovery are considered nonoperating since these are either investing, capital or noncapital financing activities. Operating expenses are all expense transactions incurred other than those related to investing, capital or noncapital financing activities and do not include interest expense and disposal of undepreciated capital assets.

NOTE 2 – BUDGETING AND BUDGETARY CONTROL

The Mill provides its own operating funds. A two-year budget appropriation is approved by the State Legislature. The Mill's budgeting is on the accrual basis. The Mill does not use encumbrance accounting.

NOTE 3 - DEPOSITS

North Dakota Century Code (NDCC) Sections 6-09-07 and 21-04-02 govern the deposit and investment of public funds.

NDCC 6-09-07 states, "All state funds…must be deposited in the Bank of North Dakota...or must be deposited in accordance with constitutional and statutory provisions."

NDCC 21-04-02 provides that public funds belonging to or in the custody of the state shall be deposited in the Bank of North Dakota.

At June 30, 2007 and 2006 the carrying amounts of the Mill's deposits were $0 and $77,856, respectively and the bank balances were $2,816,232 and $2,916,736, respectively. All deposits are exposed to custodial credit risk because they are not covered by depository insurance and the deposits are uncollateralized. These monies are deposited in the Bank of North Dakota and are guaranteed by the state of North Dakota (North Dakota Century Code Section 6-09-10).

NOTE 4 – RECEIVABLES

The Mill and Elevator entered into a note receivable with a customer in July, 2003. The total of the note was $750,000 with a variable interest rate which is the same rate that the Bank of North Dakota charges the Mill and Elevator. The note was fully paid in fiscal year 2007. The variable rate at June 30, 2006 was 6.48%, the balance was $295,100.

Receivables at June 30, 2007 and 2006 consist of the following:

June 30, 2007	Gross Receivables	Bad Debts	Billbacks/ Promotional	Net Receivables
Current Receivables				
Accounts	$ 24,748,376	$ (1,046,460)	$ (51,567)	$ 23,650,349
Margin Accounts	2,582,858			2,582,858
Other	10,000			10,000
Total Current Receivables	$ 27,341,234	$ (1,046,460)	$ (51,567)	$ 26,243,207

		Allowance		
June 30, 2006	Gross Receivables	Bad Debts	Billbacks/ Promotional	Net Receivables
Current Receivables				
Accounts	$ 21,048,450	$ (790,855)	$ (766,373)	$ 19,491,222
Margin Accounts	519,958			519,958
Other	6,667			6,667
Total Current Receivables	$ 21,575,075	$ (790,855)	$ (766,373)	$ 20,017,847

At June 30, 2007 and 2006, the ages of accounts receivable were as follows:

	2007	2006
Current	$ 15,536,963	$ 13,178,803
1-30 Days	7,239,360	6,220,801
31-60 Days	1,199,966	842,568
61-90 Days	218,264	226,186
Over 90 Days	553,823	580,092
	$ 24,748,376	$ 21,048,450

NOTE 5 - INVENTORIES

At June 30, 2007 and 2006, inventories consisted of the following:

	2007	2006
Grain	$ 12,321,393	$ 8,863,978
Flour, Feed, Resale	3,801,910	2,224,381
Supplies	413,997	350,686
Total Inventories	16,537,300	11,439,045
Less Storage Liabilities	(1,020,230)	(1,835,830)
Total	$ 15,517,070	$ 9,603,215

The Mill's net position in the grain market at June 30, 2007 and 2006 was as follows:

	2007 Bushels		2006 Bushels	
	Wheat	Durum	Wheat	Durum
Quantity on Hand	1,815,917	260,991	1,483,866	289,441
Less Storage Liability	(147,107)	(7,361)	(279,717)	(25,911)
Company Owned Grain	1,668,810	253,630	1,204,149	263,530
Open Purchase Contracts				
Cash	2,108,216	9,701	2,210,105	125,585
Futures	(2,820,000)		(1,370,000)	
Total	957,026	263,331	2,044,254	389,115
Committed to Production	(472,372)	(186,167)	(2,016,277)	(348,251)
Net Position Long (Short)	484,654	77,164	27,977	40,864

Any gains or losses on net open position would only occur if there were changes in the market price of wheat or durum prior to the Mill covering their open position. Losses on open purchase contracts could occur if there was a failure to deliver the commodity. The amount of loss would depend upon the difference between the contract price and the market price at that time.

NOTE 6 – CAPITAL ASSETS

A summary of changes in capital assets for fiscal years ended June 30, 2007 and 2006 is presented as follows:

	Balance 7/1/06	Additions	Deletions	Transfers	Balance 6/30/07
Capital Assets, Non-Depreciable:					
Land	$ 116,559			$ 104,994	$ 221,553
Construction in Progress	5,846,591	$ 3,497,347		(9,133,889)	210,048
Total Capital Assets, Non-Depreciable	$ 5,963,150	$ 3,497,347		$ (9,028,895)	$ 431,601
Capital Assets, Depreciable:					
Infrastructure	$ 1,638,588	$ 11,855			$ 1,650,443
Buildings	15,209,519			$ 2,737,367	17,946,886
Machinery & Equipment	44,160,045	30,240		6,218,629	50,408,914
Furniture & Fixtures	840,588			72,899	913,487
Total Capital Assets, Depreciable	$ 61,848,740	$ 42,095		$ 9,028,895	$ 70,919,730
Less Accumulated Depreciation for:					
Infrastructure	$ 1,494,829	$ 22,604			$ 1,517,433
Buildings	9,024,972	266,668			9,291,640
Machinery and Equipment	22,377,476	1,889,472			24,266,947
Furniture and Fixtures	721,363	34,377			755,740
Total Accumulated Depreciation	$ 33,618,640	$ 2,213,121			$ 35,831,760
Total Capital Assets, Depreciable, Net	$ 28,230,100	$ (2,171,026)		$ 9,028,895	$ 35,087,970
Capital Assets, Net	$ 34,193,250	$ 1,326,321			$ 35,519,571

	Balance 7/1/05	Additions	Deletions	Transfers	Balance 6/30/06
Capital Assets, Non-Depreciable:					
Land	$ 116,559				$ 116,559
Construction in Progress	1,695,841	$ 6,807,561	$ (2,141)	$ (2,654,670)	5,846,591
Total Capital Assets, Non-Depreciable	$ 1,812,400	$ 6,807,561	$ (2,141)	$ (2,654,670)	$ 5,963,150
Capital Assets, Depreciable:					
Infrastructure	$ 1,638,588				$ 1,638,588
Buildings	15,209,519				15,209,519
Machinery and Equipment	42,357,434	$ 55,020	$ (829,776)	$ 2,577,367	44,160,045
Furniture and Fixtures	804,959		(41,674)	77,303	840,588
Total Capital Assets, Depreciable	$ 60,010,500	$ 55,020	$ (871,450)	$ 2,654,670	$ 61,848,740
Less Accumulated Depreciation for:					
Infrastructure	$ 1,469,584	$ 25,245			$ 1,494,829
Buildings	8,735,349	289,623			9,024,972
Machinery & Equipment	21,266,616	1,906,999	$ (796,139)		22,377,476
Furniture & Fixtures	719,935	43,102	(41,674)		721,363
Total Accumulated Depreciation	$ 32,191,484	$ 2,264,969	$ (837,813)		$ 33,618,640
Total Capital Assets, Depreciable, Net	$ 27,819,016	$ (2,209,949)	$ (33,637)	$ 2,654,670	$ 28,230,100
Capital Assets, Net	$ 29,631,416	$ 4,597,612	$ (35,778)		$ 34,193,250

Depreciation expense at June 30, 2007 and 2006 was charged in the following amounts to operating expense:

	2007	2006
Manufacturing	$ 2,202,459	$ 2,253,470
General & Administrative	10,662	11,499
Total	$ 2,213,121	$ 2,264,969

NOTE 7 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2007 and 2006 were as follows:

	2007	2006
Accounts Payable	$ 1,929,523	$ 3,109,467
Accrued Gain Sharing	453,105	456,566
Accrued Payroll	108,883	109,519
Compensated Absences, Current Portion	34,354	30,924
Grain Contracts Payable	475,431	227,689
Accrued Commissions	43,212	22,080
Accrued Payroll Taxes and Benefits	320,085	344,612
Other	384,838	167,329
Total accounts payable and accrued liabilities	$ 3,749,431	$ 4,468,186

NOTE 8 – SHORT-TERM NOTES PAYABLE

The Mill uses a revolving line of credit to finance current operations. Short-term debt activity for the years ended June 30, 2007 and 2006 was as follows:

	Balance 7/1/06	Draws	Repayments	Balance 6/30/07
Line of credit	$ 4,600,000	$ 21,900,000	$ (9,500,000)	$ 17,000,000

	Balance 7/1/05	Draws	Repayments	Balance 6/30/06
Line of credit	$ 7,000,000	$ 8,600,000	$ (11,000,000)	$ 4,600,000

NOTE 9 – LONG-TERM LIABILITIES

A summary of changes in the long-term liabilities for June 30, 2007 and 2006 is presented as follows:

	Balance 7/1/06	Additions	Reductions	Balance 6/30/07	Current Portion
Net Pension Obligations		$ 476,281	$ (476,281)		
Compensated Absences	$ 672,257	373,989	(359,172)	$ 687,074	$ 34,354
Total Long-Term Liabilities	$ 672,257	$ 850,270	$ (835,453)	$ 687,074	$ 34,354

	Balance 7/1/05	Additions	Reductions	Balance 6/30/06	Current Portion
Net Pension Obligations		$ 453,199	$ (453,199)		
Compensated Absences	$ 656,909	357,349	(342,001)	$ 672,257	$ 30,924
Total Long-Term Liabilities	$ 656,909	$ 810,548	$ (795,200)	$ 672,257	$ 30,924

NOTE 10 – BONUS AND OTHER EMPLOYEE AGREEMENTS

The general manager's annual bonus opportunity is based on performance, up to 30% of base salary. The employee's annual bonus opportunity is based on achieving production, safety, and profit goals. Production and safety goals have a 4% bonus potential and if profit before gain sharing exceeds $2 million, the profit bonus would be 1% of base salary for each million in profits, or fraction thereof. The bonus potential was accrued. (See Note 7).

The head miller entered into a $20,000 promissory note with the Mill. The Mill agreed to forgive 1/3 of the note annually beginning February 23, 2005 for as long as he remains an active employee of the Mill and does not voluntarily terminate employment or was not terminated for cause by the Mill prior to February 23, 2007. Employment was terminated prior to February 23, 2007 and 1/3 of the promissory note was repaid.

The Mill entered into a $10,000 promissory note with the newly hired head miller. The Mill agreed to forgive 1/2 of the note annually beginning March 12, 2008 for as long as he remains an active employee of the Mill and does not voluntarily terminate employment or was not terminated for cause by the Mill prior to March 12, 2009.

NOTE 11 – LEASE OBLIGATIONS

During the fiscal years ended June 30, 2007 and 2006 the Mill had operating leases with original terms of 5 to 21 years on 437 and 359 bulk rail and box cars, respectively. Contract rental charges per car varied from $175 to $895 per month. The Mill also has an operating lease with Pitney Bowes for a postage machine and GMAC for the general manager's automobile. The annual contract expenses for the years ended June 30, 2007 and 2006 are as follows:

	2007	2006
Bulk rail cars	$ 3,248,474	$ 3,016,765
Postage machine	2,652	2,652
Automobile	8,603	7,135
Total operating lease payments	$ 3,259,729	$ 3,026,552

The minimum future lease payments for each of the next five years and in the aggregate is as follows:

6/30/2008	$ 3,038,390
6/30/2009	2,669,651
6/30/2010	1,872,054
6/30/2011	1,393,395
6/30/2012	1,016,920
6/30/2013-2017	1,856,300
	$ 11,846,710

NOTE 12- PENSION AND POST-RETIREMENT PLANS/BENEFITS

The North Dakota Mill and Elevator Association participates in the North Dakota Public Employees' Retirement System (NDPERS), administered by the state of North Dakota. The following is a brief description of the plans:

A. Description of Pension Plans

1. NDPERS has a cost-sharing multiple-employer defined benefit pension plan covering substantially all classified employees of the Mill. The plan provides retirement, disability and death benefits. If an active employee dies with less than three years of credited service, a death benefit equal to the value of the employee's accumulated contributions, plus interest, is paid to the employee's beneficiary. If the employee has earned more than three years of credited service, the surviving spouse will be entitled to either a single payment refund, life-time monthly payments in an amount equal to 50% of the employee's accrued normal retirement benefit, or 60 monthly payments equal to the employee’s accrued normal retirement benefit calculated as if the employee were 65 the day before death occurred, or monthly payments in an amount equal to the employees’ accrued 100% joint and survivor retirement benefit, if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the employee's accumulated pension benefits are paid; the balance will be payable to the surviving spouse's designated beneficiary.

   Eligible employees who become totally disabled after a minimum of 180 days of service receive monthly disability benefits that are equal to 25% of their final average salary, with a minimum benefit of $100. To qualify under this section, the employee must meet the criteria established by the Retirement Board for being considered totally disabled.

   Employees are entitled to unreduced monthly pension benefits beginning when the sum of age and years of credited service equal or exceed 85, or at normal retirement age (65), equal to 2% of their final average salary for each year of service. The plan permits early retirement at ages 55-64, with three or more years of service.

2. NDPERS has a cost-sharing multiple-employer defined contribution pension plan covering selected non-classified employees of the Mill. The employee selects where all mandatory contributions will be invested, from the investment options available through the plan. The plan provides retirement, disability, and death benefits. An employee gradually vests in the employer contributions as follows: 50% after two years of service; 75% after three years of service; and 100% after four years of service. An employee is always vested in their own contributions. If an active employee dies, the surviving spouse or beneficiary will receive the full market value of the vested portion of the account.

   Employees who become disabled are eligible to draw from their account until the funds are gone, subject to income taxes upon withdrawal.

   Employees are entitled to their plan benefits at any time upon separation from the state. An early withdrawal penalty may apply, if the employee takes their money before age 59½ without, for example, rolling the money into another qualified plan or IRA.

B. <u>Pension Plan Funding Policy</u>
NDPERS is funded by employee contributions (set by statute) of 4% of regular compensation. During the 1983-1985 biennium the state implemented the employer pickup provision of the IRS code whereby a portion or all of the required employee contributions are made by the employer. The state is paying the full employee contribution. Employer contributions of 4.12% of covered compensation are set by statute. The required contributions are determined using an entry age normal actuarial funding method.

C. <u>State Group Health Plan</u>
Section 54-52.1-03.2 of the North Dakota Century Code establishes a Retiree Health Benefits Fund to provide members who receive retirement benefits from the Public Employees Retirement System a credit toward their monthly health insurance premium under the state health plan based upon the member's years of credited service. The employer contribution for the Public Employees Retirement System is set by statute on an actuarially determined basis (projected unit actuarial cost method) at 1% of covered compensation. Employees participating in the retirement plan, as part-time/temporary members are required to contribute 1% of their covered compensation to the Retiree Health Benefits Fund.

The North Dakota Retirement Board was created by the state legislature and is the governing authority of NDPERS. Benefit and contribution provisions are administered in accordance with chapter 54-52 of the North Dakota Century Code. The Mill's required and actual contributions to NDPERS for the fiscal years ending June 30, 2007, 2006, and 2005 were $476,281, $453,199, and $428,669, respectively.

NDPERS issues a publicly available financial report that includes financial statements and the required supplementary information for NDPERS. The report may be obtained by writing to: NDPERS; 400 East Broadway, Suite 505; PO Box 1657; Bismarck, ND 58502-1657.

NOTE 13 - DEFERRED COMPENSATION PLAN

The state offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all state employees, permits them to defer a portion of their current salary until future years. Participation in the plan is optional. The deferred compensation is not available to the employees until separation of employment, unforeseeable emergency, deminimus distribution or qualified domestic relations orders.

All compensation deferred under the plans, all property and rights purchased with those amounts, and all income attributable to those amounts, property or rights are held in trust for the exclusive use of the employee or their beneficiary.

The North Dakota Mill and Elevator employee deposits to deferred compensation for June 30, 2007 and 2006 were $133,660 and $124,034, respectively.

NOTE 14 - CONCENTRATIONS

The Mill sells a substantial portion of its product to five major customers. Sales to these customers totaled approximately 5,688,863 and 4,888,129 hundredweight for the years ended June 30, 2007 and 2006, respectively. For the years ended June 30, 2007 and 2006, these sales were approximately 57 and 52 percent of total sales, respectively.

Approximately 67% of employees are employed under a four-year bargaining agreement that expires at June 30, 2009. This contract contains a provision that states there shall be no strikes, slowdowns or stoppages of work, picketing, boycotts, or other interference with the full operations of the business of the Company by the employees covered by this agreement and there shall be no lockout by the employer.

NOTE 15 - RELATED PARTY TRANSACTIONS

The 2005 North Dakota legislature appropriated $5,000,000 for the state general fund, $73,650, or so much of the sum as may be necessary, for the North Dakota Industrial Commission and $200,000 to the international business and trade office for the biennium beginning July 1, 2005 and ending June 30, 2007.

As referred to in Note 3, the Mill does all of its banking with the Bank of North Dakota. The Mill has established a revolving line of credit with the Bank of North Dakota and as of June 30, 2007 and 2006, there was $17,000,000 and $4,600,000 outstanding, respectively. The interest rate is variable at 1.0% over the 3-month LIBOR, adjusted quarterly for both fiscal years.

NOTE 16 - COMMITMENTS AND CONTINGENCIES

The Mill has entered into futures contracts for spring wheat to lock in a price for a future delivery or settlement period. These contracts are entered into to protect the Mill against price fluctuations of the commodity and are not reflected on the face of the financial statements. The price protection is needed to cover any long or short positions compared to flour sales. All trades are completed using two different national brokerage firms on the Minneapolis Grain Exchange. The following table shows the Mill's futures position at June 30, 2007 and 2006. One contract equals 5,000 bushels.

Futures month	Number of contracts		June 30, 2007	
	Long	Short	Avg Price	Fair Value
September		446	$ 5.629	$ 6.243
December		118	$ 5.442	$ 6.320

Futures month	Number of contracts		June 30, 2006	
	Long	Short	Avg Price	Fair Value
September		167	$ 4.700	$ 4.930
December		59	$ 4.580	$ 4.990
March		48	$ 4.900	$ 5.025

At June 30, 2007 and 2006, the Mill had committed to purchase 2,108,216 and 2,210,105 bushels of spring wheat, respectively, and 9,701 and 125,585 bushels of durum, respectively.

In addition, at June 30, 2007 and 2006, construction commitments totaled $364,952 and $1,663,410, respectively; amounts authorized totaled $575,000 and $7,510,000, respectively; and amounts expended totaled $210,048 and $5,846,590, respectively.

NOTE 17 - RISK MANAGEMENT

The North Dakota Mill and Elevator Association is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the North Dakota Mill and Elevator Association carries liability insurance and property insurance through the state's Risk Management Fund (RMF) and commercial insurance, respectively.

The 1995 Legislative Session established the RMF, an internal service fund, to provide a self-insurance vehicle for funding the liability exposures of state agencies resulting from the elimination of the state's sovereign immunity. The RMF manages the tort liability of the state, its agencies, and employees. All state agencies participate in the RMF and each fund's contribution was determined using a projected cost allocation approach.

The Mill participated in the North Dakota Worker's Compensation Bureau, an enterprise fund of the state of North Dakota. The Bureau is a state insurance fund and a 'no fault' insurance system covering the state's employers and employees financed by premiums assessed to employers. The premiums are available for the payment of claims to employees injured in the course of employment.

There have been no significant reductions in insurance coverage from the prior years and settled claims resulting from these risks have not exceeded insurance coverage in any of the past three years.